Supreme Court, U.S.
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No.

IN THE

Supreme Court of the United States

October Term, 1995

UNITED STATES OF AMERICA, *EX REL.*
JAMES M. HAGOOD,

Petitioner,

vs.

SONOMA COUNTY WATER AGENCY,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

Supplemental Appendix to Petition for Writ of Certiorari

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FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA, ex rel. JAMES M. HAGOOD, *Plaintiff/Appellant,* v. SONOMA COUNTY WATER AGENCY, *Defendant/Appellee.*	No. 89-16290 D.C. No. CV-88-0991-EFL
JAMES M. HAGOOD, *Plaintiff/Appellant,* v. SONOMA COUNTY WATER AGENCY, *Defendant/Appellee.*	No. 89-16360 D.C. No. CV-88-0991-EFL OPINION

Appeal from the United States District Court
for the Northern District of California
Eugene F. Lynch, District Judge, Presiding

Argued and Submitted
February 15, 1991—San Francisco, California

Filed April 2, 1991

Before: Mary M. Schroeder, William C. Canby, Jr. and
John T. Noonan, Jr., Circuit Judges.

Opinion by Judge Noonan

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OPINION

NOONAN, Circuit Judge:

James M. Hagood brought suit under the qui tam provision of the False Claims Act, 31 U.S.C. §§ 3729-3733, alleging its violation by the Sonoma County Water Agency (the Water Agency). The district court dismissed his third amended complaint for failure to state a cause of action. On appeal, the United States filed a brief as amicus curiae, arguing that the district court was incorrect in its reasoning but right in its result, because the court had no jurisdiction of Hagood's complaint. The jurisdictional issue is novel. We decide it in favor of jurisdiction and reverse the district court on the question of whether Hagood stated a cause of action.

BACKGROUND

In February 1982, as the attachments to Hagood's complaint make clear, Hagood was assistant district counsel to the San Francisco District of the Army Corps of Engineers (the

Corps) and was assigned to represent the district counsel to handle the renegotiation of the Warm Springs Dam Water Supply contract with the Water Agency. Hagood came to the conclusion that the proposed cost allocations for the new contract, which would govern the Water Agency's repayment obligations, did not comply with the terms of the 1958 Water Supply Act, 43 U.S.C. § 390b. The cost allocations proposed by the Corps substantially reduced the obligations of the Agency.

Hagood — again according to the documents attached to his complaint — brought his objections to Colonel Paul Bazilwick, Jr., the District Engineer and Contracting Officer for the project. Bazilwick made what he termed "a command decision" to proceed with the cost allocations as proposed and to accept responsibility for the clauses in the contract to which Hagood had objected. Hagood orally refused to draft the contract in this form. He then received an order from the district counsel to comply with Colonel Bazilwick's order or "suffer the consequences of a refusal to follow a direct order from an individual within your direct chain of command."

On March 25, 1982, Hagood put his legal objections to the contract in writing in a letter addressed to Colonel Bazilwick with carbon copies to various other officers of the Corps. The district counsel responded with a memorandum for the files, disputing Hagood's legal points and specifically arguing that the 1958 Water Supply Act did not apply to the Warm Springs Dam, which had been authorized by Congress in 1962. The memorandum of district counsel concluded that Hagood's personal opinion was not the opinion of legal counsel for the district.

According to the allegations of the complaint, Bazilwick was "in the spring" seeking a job with a company later awarded design work by the Water Agency on the Warm Springs Dam and he "used his position as District Engineer to cause an obstruction as to Hagood raising the most fundamental questions on the purported repayment arrangement. A product of that was threats received by Hagood which basically indicated if you want

your job with Army Corps in San Francisco don't ask any questions."

Meanwhile, the contract that Hagood had refused to prepare had been prepared. According to the allegations of the complaint, the Water Agency "used pressure and influence" to expedite its signing without accurate and current cost allocations. The signatory for the Army was William Gianelli, Assistant Secretary of the Army. According to the complaint, Gianelli had been Director of Water Resources for the State of California, had been involved in that capacity with the Warm Springs Dam, and therefore had "a conflict of interest" in acting on the contract. He knew that "an accurate and current cost allocation" had not been prepared, and this knowledge "is related to his expediting" of the contract. The contract was signed by Gianelli on October 1, 1982.

According to the complaint's allegations, the district counsel advised Hagood in April 1982 "that he was no longer considered an attorney in the San Francisco district," and Hagood was told by unnamed other Corps lawyers that "he had better get out of California." In July 1982 Hagood "found a job in Alaska with the Army Corps." It appears from other parts of the complaint that Hagood's new job was as assistant district counsel in Anchorage. In 1985 he transferred to the Sacramento district of the Corps. In 1987 he retired.

PROCEEDINGS

Pursuant to 31 U.S.C. § 3730(b), Hagood began this suit for himself and for the United States in March 1988. The United States declined to proceed with the suit on its own behalf, but invoking 31 U.S.C. § 3730(c)(2)(A) intervened to ask dismissal of the complaint's claims against two individual defendants, Colonel Bazilwick and the San Francisco district counsel. This motion was granted. Hagood proceeded as the sole plaintiff as provided by 31 U.S.C. § 3730(c)(3). He amended his complaint

so that it named only the Water Agency. The defendant moved to dismiss. The motion was granted with leave to amend.

Hagood's third amended complaint alleged that the Water Agency "knowingly presented, caused to be presented and conspired to present the following false information," to wit, "that a true and correct, and current and accurate cost allocation was contained in the 1982 contract," and various other misstatements and material omissions relating to the contract. The resulting damage to the United States was asserted to be at least $60 million. The Water Agency was further charged, as already noted, with using pressure and influence to expedite the signing of the contract based on this false information.

After a hearing, the district court on September 25, 1989 dismissed with prejudice Hagood's third amended complaint for failure to state a claim for which relief could be granted. In a memorandum opinion the district court analyzed Hagood's complaint as essentially self-contradictory: the complaint alleged fraud by the defendant but also alleged that "the high government officials responsible for taking the action" knew of the facts that made the complaint false. The complaint failed to charge, "with the specificity necessary under Rule 9(b) of the Federal Rules of Civil Procedure," these officials with "acting with any fraudulent intent" toward the government. The district court observed that the closest Hagood came to alleging fraud was his allegations about Bazilwick and Gianelli but that Hagood made "no connection between these allegations and any direct form of wrongdoing by the government employees."

The district court found the facts to be similar to those of *Boisjoly v. Morton Thiokol, Inc.*, 706 F. Supp. 795, 808-10 (D. Utah 1988), and so came to the same conclusion as *Boisjoly*, that it was impossible to say that the government had suffered the kind of injury necessary to impose liability under the False Claims Act. In amplification of this conclusion, the court observed that the United States is not necessarily damaged every time its officers agree to a procedure that diminishes money coming into the Treasury, because the officers may have acted to

promote non-monetary interests of the United States — for example, here, to increase water storage facilities. Moreover, the court noted, "it is difficult to see how any damages to the United States are caused by false statements when officials, with full knowledge of the falsity of the statements, proceed to take an action depriving the government of funds notwithstanding the false statements."

Hagood appealed to this court. The United States was permitted to file a brief amicus curiae. This brief argued that the district court was mistaken in its reasoning for two reasons: under the False Claims Act penalties are recoverable even if the United States sustains no damage from the false claim; and the government's knowledge of a claim's falsity does not preclude recovery. At the same time the brief contended that the district court lacked jurisdiction of Hagood's claim because of "the plain language" of 31 U.S.C. § 3730(e)(4).

ANALYSIS

Jurisdiction. Exclusions of federal jurisdiction, set out in the 1986 amendments to the False Claims Act, are unusually precise:

> No court shall have jurisdiction over an action brought by a former or present member of the armed forces . . . against a member of the armed forces arising out of such person's service in the armed forces. 31 U.S.C. § 3730(e)(1)
>
> No court shall have jurisdiction over an action brought under subsection (b) against a Member of Congress, a member of the judiciary, or a senior executive branch official if the action is based on evidence or information known to the Government when the action was brought. *Id.* (e)(2)(A).

> No court shall have jurisdiction over an action under this section based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government Accounting Office report, hearing, audit, or investigation, or from the news media, unless the action is brought by the Attorney General or the person bringing the action is an original source of the information. *Id.* (e)(4)(A).
>
> For purposes of this paragraph, "original source" means an individual who has direct and independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the Government before filing an action under this section which is based on the information. *Id.* (e)(4)(B).

[1] The jurisdictional bar that the United States contends is applicable is the last. The United States argues that when Hagood became involved in preparation of the disputed contract he was engaged in an "administrative investigation," so that the words of the statutory exclusion are met. The United States further argues that the "public disclosure" required by the statute occurred when Hagood as a government employee "disclosed" to himself as a member of the public the information on which he based his suit.

To say that the argument of the United States is tortured is to state the obvious. Even if we were to construe "investigation" broadly, as the United States argues, it requires a major extension of the term to hold that it includes the preparation of a contract by a lawyer. Without deciding whether such a liberal extension of the statutory language should be made, we hold that no "public disclosure" was made. The public disclosure that the statute requires is public disclosure *in* an administrative investigation. The United States concedes that one government employee telling another government employee is *not* public disclosure. The notion that we should subdivide Hagood into his

governmental self and his nongovernmental self is too metaphysical a contention for the interpretation of a plain congressional enactment. Hagood does not base his suit on any public disclosure made to him or to anyone else. He bases his suit on information that he acquired in preparing the contract; the information was not publicly disclosed.

The United States has neither case law nor legislative history to support its extraordinary reading of a remarkably explicit jurisdictional statute. We join the First Circuit in rejecting the government's position. *United States ex rel, LeBlanc v. Raytheon Co.*, 913 F.2d 17 (1st Cir. 1990).

Basically the United States takes its position in surprise and chagrin at a change in the law made by the 1986 amendments. Although it is not strictly necessary to our decision, we review the history that appears to account for the government's present position. In *United States ex rel Marcus v. Hess*, 317 U.S. 537, 63 S.Ct. 379, 87 L. Ed. 443 (1943), it was held that an informer might recover in a qui tam action under the False Claims Act even if he had "contributed nothing" to the discovery of the fraud but had derived all his information from the government's criminal indictment that set out all the facts now relied on in the qui tam action. The Court noted that under the terms of the act "any person" could bring a suit and that the Senate sponsor of the law had observed that even a district attorney, deriving all his knowledge from his official position, could bring a qui tam suit under the law. *Id.* at 546, 63 S.Ct. at 385. The government objected to such a construction of the law with objections of policy. The Court told the government its objections should be addressed to Congress: "the entire force of these considerations is directed solely at what the government thinks Congress should have done rather than at what it did." *Id.* at 546-547, 63 S.Ct. at 385.

Immediately after *Hess* was decided, Congress did amend the law to exclude "parasitical suits," i.e., those where the government already possessed the information underlying the qui

tam action. "The court shall have no jurisdiction," the amendment provided, "whenever it shall be made to appear that such suit was based upon evidence or information in the possession of the United States, or any agency, officer, or employee thereof, at the time such suit was brought." 31 U.S.C. § 232(C)(1976). If this language were in place today, Hagood would be barred. *Pettis ex rel. United States v. Morrison-Knudsen Co.,* 577 F.2d 668 (9th Cir. 1978). But this language disappeared from the statute with the 1986 amendments.

Citing S.Rep. No. 345, 99th Cong., 2d Sess. (1986), U.S. Code Cong. Admin. News 1986, p. 5266, the United States concedes that the purpose of the 1986 amendments was to repeal overly-restrictive court interpretations of the qui tam statute, which had prohibited not only suits by private citizens based on information obtained by the government, but also suits brought by those who had information independently of the government. Clearly, however, what Congress found overly-restrictive interpretation went further than what the government now finds desirable. The new jurisdictional bars were carefully crafted. They were framed by those surely aware of *Hess,* its holding that "any person" means "any person," and its declaration that arguments about the limits on suits by informers should be addressed to Congress not the courts. All that was said in *Hess* is true here. The government has some good policy arguments. "But the trouble with these arguments is that they are addressed to the wrong forum." *Hess,* 317 U.S. at 547, 63 S.Ct. at 386.

There is, of course, no need for Hagood to show that he is "the original source" of the information. That statutory phrase in 31 U.S.C. § 3730(e)(4)(B) comes into play only if an exception is sought to the bar of 4(A). As the bar of 4(A) does not apply, there is no need to invoke the exception.

The Sufficiency of the Complaint. In so many words, Hagood alleges that the Water Agency knowingly presented and caused to be presented and conspired to present a false claim. That a contract based on false information is a species of false claim is undisputed. The contention of the Water Agency, relying on the

district court's opinion, is that Hagood's charge is negated by the rest of his complaint which says that the relevant government officials knew that the information was false.

[2] Aided by the brief of the United States, of which the district court did not have the benefit, we hold that Hagood has not engaged in an exercise of self-contradiction. To be sure, he comes very close to it, especially when the documents annexed to his complaint are considered, for in them it appears that the contract was prepared not by the Water Agency but by the Corps. Nonetheless, reading the complaint generously, as our precedents dictate should be done, it is evident that what the complaint alleges is that the Water Agency played an active part in having presented for signature a contract that the Water Agency knew was based on false information.

What is crucial — and what must be proven at trial—is that the Water Agency knew that the information was false. The statute emphasizes that the act, for which the civil claim may be filed is to "knowingly" present or cause to be presented "a false or fraudulent claim," 31 U.S.C. § 3729(a)(1), or to "knowingly" make, use or cause a false record or statement to be made to get a false or fraudulent claim paid. *Id.* (a)(2), or to "knowingly" make, use, or cause a false record or statement to be made to "decrease an obligation" to pay the government. *Id.* (a)(7). The emphasis on "knowing" and "knowingly" is reinforced by their statutory definitions. *Id.* (b).

[3, 4] Innocent mistake is a defense to the criminal charge or civil complaint. So is mere negligence. The statutory definition of "knowingly" requires at least "deliberate ignorance" or "reckless disregard." To take advantage of a disputed legal question, as may have happened here, is to be neither deliberately ignorant nor recklessly disregardful. But that the Water Agency did no more than that cannot be determined from the complaint.

[5] That a defendant has disclosed all the underlying facts to the government may, the United States in its brief concedes, show that the defendant had no intent to deceive. But what

constitutes the offense is not intent to deceive but knowing presentation of a claim that is either "fraudulent" or simply "false." 31 U.S.C. § 3729(a)(1) and (2). The requisite intent is the knowing presentation of what is known to be false. That the relevant government officials know of the falsity is not in itself a defense, *United States v. Ehrlich,* 643 F.2d 634, 638-639 (9th Cir. 1981). *Boisjoly* may be defensible on its facts; its dicta are an unreliable guide.

As the brief of the United States points out, the knowledge possessed by officials of the United States may be highly relevant. Such knowledge may show that the defendant did not submit its claim in deliberate ignorance or reckless disregard of the truth. But this comforting conclusion for the Water Agency cannot be reached by mere inspection of Hagood's complaint. Only at the stage of trial or summary judgment will it be possible for a court to say, for example, that the Water Agency did merely what the Corps bid it do, that the Water Agency had no knowledge that its contract was based on what Hagood has alleged was false information.

The damages sustained by the United States also can not be determined from the complaint. It may be, as the district court observed, that no damages were suffered when officers of the United States knowledgeably decided to proceed with the contract. The complaint alone does not say what the balance of benefits and harms was; it alleges damages of $60 million. If such damages are shown to have occurred by reason of a false claim, it would be for the defendant to show how they were offset.

[6] A civil penalty of between $5,000 and $10,000, and the costs of the civil action, are also recoverable under the statute, 31 U.S.C. § 3729(a). No damages need be shown in order to recover the penalty. *See Rex Trailer Co. v. United States,* 350 U.S. 148, 153, n.5, 76 S.Ct. 219, 222, n.5, 100 L.Ed. 149 (1956).

[7,8] *Estoppel.* Estoppel is an affirmative defense, Fed. R. Civ. Proc. 8(c). It was not here pleaded. If the opinion of the district court is construed as holding that the United States was

estopped by the knowledge of its officers, the district court's opinion would rely on a defense not before it. In any event, estoppel will not lie against the United States "on the same terms as any other litigant." *Heckler v. Community Health Services,* 467 U.S. 51, 60, 104 S.Ct. 2218, 2224, 81 L.Ed.2d 42 (1984). The defendant's "inability to retain money that it should never have received in the first place" is not the kind of detrimental reliance that justifies estoppel against the government. *Id.* at 61. Such is just this case, if Hagood's allegations prove to be good. "Protection of the public fisc requires that those who seek public funds act with scrupulous regard for the requirements of the law . . . [T]hose who deal with the Government are expected to know the law and may not rely on the conduct of Government agents contrary to law." *Id.* at 63. Hagood claims that the Water Agency proceeded unscrupulously, indeed with knowledge of the falsity of its claim, with knowledgeable government officials abetting its behavior. Hagood's allegations constitute a cause of action.

REVERSED and REMANDED.

ENTERED IN CIVIL DOCKET 9-10-1989

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

UNITED STATES OF AMERICA, ex rel, JAMES M. HAGOOD, *Plaintiff,* vs. SONOMA COUNTY WATER AGENCY, *Defendant.*	No. C-88-0991-EFL MEMORANDUM OPINION

James Hagood brought this action against the Sonoma County Water Agency ("the Agency") on behalf of the United States as a plaintiff *qui tam* pursuant to the False Claims Act, 31 U.S.C. § 3729, et seq. ("the Act"). Hagood, who is proceeding *in propria persona*, alleges in his third amended complaint that the Agency knowingly submitted false claims to the United States with regard to its repayment obligations on a dam project constructed by the Army Corps of Engineers ("the Corps"). The Agency moved to dismiss the complaint with prejudice for failure to state a claim pursuant to Federal Rule of Civil Procedure 12(b)(6). The Court granted the Agency's motion at a hearing on August 28, 1989 and subsequently entered judgment in favor of the Agency on September 25, 1989. The basis for this judgment is set forth in this opinion.

I. *PROCEDURAL BACKGROUND*

Hagood filed his original complaint in this case on March 22, 1988, naming the Agency and two individual federal government employees as defendants. The matter was ordered sealed to allow the United States to determine whether to intervene in the action under section 3730 of the Act. On November 28, 1988, the United States decided to intervene only to have the action dismissed against the individual defendants. The Court granted the motion to dismiss the individual defendants on March 7, 1989 and ordered the seal lifted.

Hagood, proceeding *qui tam* under section 3730 of the Act, filed his second amended complaint, naming only the Agency as defendant. The Agency moved to dismiss this complaint. This motion was granted with leave to amend on May 30, 1989. After substituting himself as counsel, Hagood filed a third amended complaint against the Agency, which again moved for dismissal with prejudice. The Court granted this motion orally on August 28, 1989 and entered judgment for the Agency on September 25, 1989. The Court's reasoning in granting the motion to dismiss with prejudice is as follows.

II. *FACTS AS ALLEGED IN THE COMPLAINT*

Hagood's charge of wrongdoing against the Agency grows out of construction of a water storage facility in Sonoma County, California for the Agency by the Corps. Planning for the dam's construction began in 1964, when the Agency and the Corps entered into a contract for construction of a dam with water storage capacity of 132,000 acre feet ("the Dry Creek Project"). Under this contract, the Agency was to repay the Corps 29% of its construction costs based on an allocation of the expenses related to water storage. *See* 43 U.S.C. § 390(b).

In 1975, the project was modified in order to increase the water storage capacity of the dam by 60% to 212,000 acre feet ("the Warm Springs Project"). Hagood alleges that this modification was adopted by the Corps without the required submission by the Agency of an accurate cost allocation based on the larger scale of the new Warm Springs Project. He claims that the Agency's repayment obligations should have increased as a result of the modification and the failure to require a new cost allocation caused significant monetary damage to the United States.

Furthermore, Hagood alleges that in 1982 the Agency sought to decrease its repayment obligations to 27% of the total cost of the Warm Springs Project by either intentionally submitting a false cost allocation or by failing to submit one altogether, causing the United States to rely on an obsolete cost allocation made in 1969. By Hagood's estimate, a proper cost allocation

would have revealed that the Agency should have repaid the Corps for 50% of its construction costs. Hagood also alleges that the 1982 modifications to the Dry Creek agreement allowed the Agency to begin repayment ten years later than legally required and to benefit from interest deferment for a longer period than statutorily allowed.

Hagood directed the attention of his superiors in the legal counsel's office at the Corps to these alleged deficiencies in the 1982 modifications. He claims that he was ordered to draft a contract embodying the modifications notwithstanding their illegality. Upon his refusal to do so, he alleges that he was threatened by Steve Lingenfelter, the district counsel for the Corps, and Paul Bazilwich, a Colonel in the Corps. Hagood later informed army generals and a United States Senator of the irregularities, none of whom took any action. After these contacts, Hagood claims that he received phone calls from employees of the Corps threatening his personal safety. Despite his efforts, Hagood alleges that a "Mr. Gianelli," whom he identifies as an Assistant Secretary of the Army, expedited the approval of the contract with full knowledge of its legal and financial defects.

III. *HAGOOD'S FAILURE TO STATE A CLAIM UNDER THE ACT*

In ruling on a motion to dismiss for failure to state a claim, all material allegations set forth in the complaint must be accepted as true and construed in the light most favorable to the plaintiff. *NL Indus., Inc. v. Kaplan*, 792 F.2d 896, 898 (9th Cir. 1986). It appears to be the gist of Hagood's 36-page complaint that the terms of the 1982 agreement modifying the original Dry Creek repayment terms without an accurate cost allocation constitute a false claim against the United States within the meaning of the Act, costing the government some $60 million in damages. Defendant argues that the extensive information had by the government about the lack of an accurate cost allocation as alleged in Hagood's complaint precludes a finding of damage to the government, therefore calling for a dismissal of the complaint for failure to state a claim for which relief can be granted.

In order to state a claim under the Act, a *qui tam* plaintiff must plead the existence of a false claim against the United States as defined in Section 3729(a) of the Act, which reads in pertinent part:

> **Liability for certain acts.** —Any person who—
>
> (1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval;
>
> (2) knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government;
>
> (3) conspires to defraud the Government by getting a false or fraudulent claim allowed or paid;
>
> . . .
>
> (6) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the government, or a member of the Armed Forces, who lawfully may not sell or pledge the property[1];
>
> (7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government;
>
> is liable to the United States for a civil penalty . . .

Section 3730 of the Act further permits a *qui tam* plaintiff to recover an award of up to 30% of the damages and penalties

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[1] Hagood relies on this subsection in one paragraph of his third amended complaint, which alleges that failure to make the proper repayments on the water storage facilities amounts to a sale of "public property" by government officials unauthorized to make such a sale. The Court views this allegation as simply a restatement of Hagood's allegations under the other subsections of the Act and feels that the transactions involved in this case do not involve a sale of public property as meant in this subsection. As such, the Court has not considered this single allegation separately from the rest of Hagood's complaint.

assessed against the false claimant in the event that the government chooses not to intervene in the case.

Prior to 1986, Hagood's complaint would clearly have been subject to the jurisdictional bar of section 3730(b)(4), which prevented a *qui tam* plaintiff from bringing an action "based on information or evidence the government had when the action was brought." *See U.S. ex rel. Weinberger v. Florida*, 615 F.2d 1370 (5th Cir. 1980) (decided under 31 U.S.C. § 232, the predecessor to the current Act). However, Congress removed this jurisdictional bar when it amended the Act in 1986; the amended language of the Act contains the jurisdictional bar only in relation to false claim actions against members of Congress, the judiciary, or senior executive branch officials. 31 U.S.C. § 3730(e)(2)(A). The legislative history of the amendments to the Act indicates that Congress intended to "repeal[ ] the jurisdictional bar for most suits" except those "which might be politically motivated." S.Rep. No. 345, 99th Cong., 2d Sess. 29, *reprinted in* 1986 U.S. Code Cong. & Admin. News 5266, 5294. Therefore, Hagood is not *jurisdictionally* prevented from bringing this suit under the Act.[2] The Agency does not make this contention, however. Rather, the Agency argues that Hagood has failed to allege, and cannot allege, either that the United States has been damaged by the actions of the Agency or that the Agency's actions caused any damages to the United States. The crucial question before the Court in this case is whether allegations of the false claim can be actionable under the Act even with full knowledge of false statements on the part of high ranking government officials with the authority to approve the 1982 modifications to the Agency's

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[2] The Court previously ruled that the 1986 amendments to the Act applied retroactively to this case. The Court reiterates that ruling here on the basis of the weight of authority construing the amendments as retroactive. *See, e.g., United States v. Oakwood Downriver Medical Center*, 687 F. Supp. 302 (E.D. Mich. 1988); *Gravitt v. General Elec. Co.*, 680 F. Supp. 1162 (S.D. Ohio 1988); *United States v. Hill*, 676 F. Supp. 1158 (N.D. Fla. 1987); *United States v. Board of Educ. of Union City*, 697 F. Supp. 167 (W.D. Wis. 1988).

repayment terms without allegations of any conspiracy or fraudulent conduct on the part of those officials.

The 1986 amendments to the Act did not change the fact that the Act remains a statute for combatting fraud against the government. While it may not be required that Hagood plead the elements of common law fraud, the Act requires that he plead at least 1) a claim for payment against the government, and 2) that the claim is false or fraudulent. *Boisjoly v. Morton Thiokol, Inc.*, 706 F. Supp. 795, 808 (D. Utah 1988). Another court has gone even further, listing the elements of a false claim under the Act as:

> 1. The defendant presented or caused to be presented, for payment or approval, to the Government of the United States a claim upon or against the United States;
>
> 2. The claim was false or fictitious;
>
> 3. The defendant knew that the claim was false, fictitious, or fraudulent; and
>
> 4. To recover damages, *it must be shown that the United States sustained damages by reason of the false claim.*

United States v. Board of Educ. of Union City, 697 F. Supp. 167 (D.N.J. 1988)(emphasis added).[3]

Hagood has failed in his third amended complaint to properly allege the elements of a claim under the Act under either of the above standards. Where the complaint alleges on its face knowledge of the claimed false statements among high level governmental officials responsible for taking the action which allegedly causes the damage to the government, a claim under the Act is "effectively negated." *Boisjoly*, 706 F. Supp. at 809. Without any allegation of participation in the fraud against the government by the governmental officials with knowledge of the

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[3] Both Hagood and the Agency agree in their written submissions on the motion to dismiss that *Union City* properly states the requirements for a claim under the Act.

false statements, "if the complaint itself alleges that the government knew of those very facts or characteristics which allegedly make the claim false, no claim has been stated." *Id.* at 810.

In *Boisjoly*, a *qui tam* plaintiff brought an action against the manufacturer of the defective joint seals thought to be responsible for the explosion of the space shuttle Challenger. His complaint alleged that NASA had known "for years" that the joint seals were defective. *Id.* at 809. The court dismissed the plaintiff's complaint because high level governmental officials had knowledge of fraudulent statements by the defendant. On those facts, it was impossible for the court to say that the government "had suffered the kind of injury necessary to invoke [False Claim Act] liability." *Id.*

The instant case seems to fall squarely within the facts of *Boisjoly*. Hagood alleges that a number of high ranking officials in the Corps and the Army knew about the Agency's alleged false claims. For whatever reason, whether it was ignorance of the law or political expediency, those officials chose to proceed with the Warm Springs contract. Hagood has failed, and indeed refused, to plead that these officials were acting with any fraudulent intent toward the government with the specificity necessary under Rule 9(b) of the Federal Rules of Civil Procedure.[4] Rather, Hagood would have the Court find that a claim is actionable under the False Claims Act whenever fully informed high

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[4] Besides vague allegations of some sort of conspiracy throughout the complaint, Hagood makes only two specific allegations which could conceivably amount to fraudulent behavior on the part of governmental employees responsible for approving the Warm Springs contract. First, he alleges that Gianelli, as a former employee of the California Department of Water Resources, had "a conflict of interest" and should have recused himself from considering the 1982 contract. He also alleges that Bazilwich, the Army colonel who ordered Hagood to prepare the 1982 contract, was looking for a job with a private contractor involved in construction of the Warm Springs project. He makes no connection between these allegations and any direct form of wrongdoing on the part of the government employees in relation to the Warm Springs contract. As such, his complaint fails to meet the requirements of Rule 9(b).

ranking officials acting within their authority take an action which may deprive the United States Treasury of some funds.[5]

The Court refuses to accept this statement of the type of injury to the United States required to state a claim under the Act. The Court agrees with the *Union City* court, which required a showing of both damage to the United States and causation of the damage by the false statements. The United States is not necessarily damaged when its officials act, in an absence of fraudulent intent, in a way which may diminish funds coming into the Treasury, as these officials may take such action for other reasons beneficial to the United States, such as expediting the construction of increased water storage facilities. Furthermore, it is difficult to see how any damages to the United States are caused by false statements when officials, with full knowledge of the falsity of the statements, proceed to take an action depriving the government of funds notwithstanding the false statements.

For these reasons, Hagood's third amended complaint is dismissed. The Court refuses to accept Hagood's position that the removal from the Act of the "knowledge in the government" jurisdictional bar by Congress altered the underlying nature of the Act as a fraud statute. Hagood is not barred jurisdictionally from bringing this action. Rather he has failed to allege any damage or causation of such damage to the United States by the Agency's alleged false statements where highly placed governmental officials knew of the falsity of the statements, yet acted upon them anyway without an fraudulent intent.

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[5] Indeed, Hagood contended at oral argument on the motion to dismiss that he would have a claim against the Agency even if the President of the United States had approved the 1982 contract with full knowledge of the alleged misrepresentations by the Agency. He argued that section 3729(b) of the Act, which defines the terms "knowing and knowingly" as including individuals who act with "reckless disregard of the truth," would apply in this situation. A simple reading of the statute reveals that Hagood has completely missed the point of section 3729(b), which is clearly meant to apply to the party alleged to be defrauding the government, and not the government officials who act upon an alleged misstatement.

IV. *DISMISSAL OF HAGOOD'S COMPLAINT WITH PREJUDICE*

It is of course well established that a motion to dismiss a complaint should not be granted unless it appears beyond a reasonable doubt that the plaintiff can prove no set of facts which would entitle him to relief. *Conley v. Gibson,* 355 U.S. 41, 45-46 (1957). In those circumstances where a defendant has shown that a plaintiff's complaint fails to state a claim, leave to amend the defective complaint will normally be granted. As an exception to these rules, a motion to dismiss with prejudice will be granted when amending the complaint would serve no purpose or would be futile. *Havas v. Thornton,* 609 F.2d 372, 376 (9th Cir. 1979).

In this case, the Court has granted the Agency's motion to dismiss with prejudice and judgment has been entered accordingly. As discussed above, Hagood's third amended complaint failed to allege the requisite injury or causation of that injury necessary to state a claim under the Act. His second amended claim was dismissed with leave to amend on the same grounds on May 30, 1989. At a hearing on the earlier motion, the Court asked Hagood to amend his complaint to allege with more specificity the names of government officials involved in the approval of the 1982 contract, the degree of their knowledge of the alleged false statements by the Agency, and any wrongdoing or fraudulent intent on the part of those officials.

Hagood's third amended complaint was indeed more detailed, but alleged essentially the same facts. If anything, the allegations of knowledge of the false statements of particular high level officials with the power to approve the contract made the third amended complaint even more vulnerable to a motion to dismiss because, while it alleged detailed and specific knowledge of highly placed officials, it failed to sufficiently allege any wrongdoing by these government officials as requested by the Court. At oral argument on the motion, the Court repeatedly offered Hagood another opportunity to amend his complaint to include such allegations, but it became clear from Hagood's position that he would not, or could not, do so. Rather, Hagood

insisted that mere allegations of monetary loss to the United States Treasury were sufficient to state a claim under the Act.

As such, the Court dismissed Hagood's third amended complaint with prejudice because it viewed any amendment along the lines of Hagood's theory as futile, having already considered and ruled on the motion twice. Where a plaintiff seeks merely to restate previously considered claims in an amended complaint, the district court may properly deny leave to amend. *Fidelity Financial Corp. v. Federal Home Loan Bank,* 792 F.2d 1432, 1438 (9th Cir. 1986). Hagood has made his argument clear to this Court in his several "bites at the apple," and the Court views his position as legally flawed. Considering his refusal to reconsider his position and submit an amended complaint sufficiently alleging wrongdoing or fraudulent intent on the part of government officials, the Court had no choice but to issue a judgment upon dismissal of Hagood's third amended complaint.

DATED: October 16, 1989.

/s/ EUGENE F. LYNCH

EUGENE F. LYNCH
United States District Judge

FALSE CLAIMS ACT

31 U.S.C. 3729 *et seq.*

§ 3729. False claims

a) **Liability for certain acts.** Any person who—

(1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval;

(2) knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government;

(3) conspires to defraud the Government by getting a false or fraudulent claim allowed or paid;

(4) has possession, custody, or control of property or money used, or to be used, by the Government and, intending to defraud the Government or willfully to conceal the property, delivers, or causes to be delivered, less property than the amount for which the person receives a certificate or receipt;

(5) authorized to make or deliver a document certifying receipt of property used, or to be used, by the Government and, intending to defraud the Government, makes or delivers the receipt without completely knowing that the information on the receipt is true;

(6) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge the property; or

(7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government,

is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000, plus 3 times the amount of damages which the Government sustains because of the act of that person, except that if the court finds that—

(A) the person committing the violation of this subsection furnished officials of the United States responsible for investigating false claims violations with all information known to such person about the violation within 30 days after the date on which the defendant first obtained the information;

(B) such person fully cooperated with any Government investigation of such violation; and

(C) at the time such person furnished the United States with the information about the violation, no criminal prosecution, civil action, or administrative action, had commenced under this title with respect to such violation, and the person did not have actual knowledge of the existence of an investigation into such violation;

the court may assess not less than 2 times the amount of damages which the Government sustains because of the act of the person. A person violating this subsection shall also be liable to the United States Government for the costs of a civil action brought to recover any such penalty or damages.

(b) **Knowing and knowingly defined.** For purposes of this section, the terms "knowing" and "knowingly" mean that a person, with respect to information—

(1) has actual knowledge of the information;

(2) acts in deliberate ignorance of the truth or falsity of the information; or

(3) acts in reckless disregard of the truth or falsity of the information

and no proof of specific intent to defraud is required.

(c) **Claim defined.** For purposes of this section, "claim" includes any request or demand, whether under a contract or otherwise, for money or property which is made to a contractor, grantee, or other recipient if the United States Government provides any portion of the money or property which is requested or demanded, or if the Government will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded.

(d) **Exemption from disclosure.** Any information furnished pursuant to subparagraphs (A) through (C) of subsection (a) shall be exempt from disclosure under section 552 of title 5.

(e) **Exclusion.** This section does not apply to claims, records, or statements made under the Internal Revenue Code of 1954. (As amended Oct. 27, 1986. P. L. 99-562, § 2. 100 Stat. 3153.)

§ 3730. Civil actions for false claims

(a) **Responsibilities of the Attorney General.** The Attorney General diligently shall investigate a violation under section 3729. If the Attorney General finds that a person has violated or is violating section 3729, the Attorney General may bring a civil action under this section against the person.

(b) **Actions by private persons.** (1) A person may bring a civil action for a violation of section 3729 for the person and for the United States Government. The action shall be brought in the name of the Government. The action may be dismissed only if the court and the Attorney General give written consent to the dismissal and their reasons for consenting.

(2) A copy of the complaint and written disclosure of substantially all material evidence and information the person possesses shall be served on the Government pursuant to Rule 4(d)(4) of the Federal Rules of Civil Procedure. The complaint shall be filed in camera, shall remain under seal for at least 60 days, and shall not be served on the defendant until the court so orders. The Government may elect to intervene and proceed with the action within 60 days after it

receives both the complaint and the material evidence and information.

(3) The Government may, for good cause shown, move the court for extensions of the time during which the complaint remains under seal under paragraph (2). Any such motions may be supported by affidavits or other submissions in camera. The defendant shall not be required to respond to any complaint filed under this section until 20 days after the complaint is unsealed and served upon the defendant pursuant to Rule 4 of the Federal Rules of Civil Procedure.

(4) Before the expiration of the 60-day period or any extensions obtained under paragraph (3), the Government shall—

(A) proceed with the action, in which case the action shall be conducted by the Government; or

(B) notify the court that it declines to take over the action, in which case the person bringing the action shall have the right to conduct the action.

(5) When a person brings an action under this subsection, no person other than the Government may intervene or bring a related action based on the facts underlying the pending action.

(c) **Rights of the parties to qui tam actions.** (1) If the government proceeds with the action, it shall have the primary responsibility for prosecuting the action, and shall not be bound by an act of the person bringing the action. Such person shall have the right to continue as a party to the action, subject to the limitations set forth in paragraph (2).

(2)(A) The Government may dismiss the action notwithstanding the objections of the person initiating the action if the person has been notified by the Government of the filing of the motion and the court has provided the person with an opportunity for a hearing on the motion.

(B) The Government may settle the action with the defendant notwithstanding the objections of the person initiating the action if the court determines, after a hearing, that the proposed settlement is fair, adequate, and reasonable under all the circumstances. Upon a showing of good cause, such hearing may be held in camera.

(C) Upon a showing by the Government that unrestricted participation during the course of the litigation by the person initiating the action would interfere with or unduly delay the Government's prosecution of the case, or would be repetitious, irrelevant, or for purposes of harassment, the court may, in its discretion, impose limitations on the person's participation such as—

(i) limiting the number of witnesses the person may call;

(ii) limiting the length of the testimony of such witnesses;

(iii) limiting the person's cross-examination of witnesses; or

(iv) otherwise limiting the participation by the person in the litigation.

(D) Upon a showing by the defendant that unrestricted participation during the course of the litigation by the person initiating the action would be for purposes of harassment or would cause the defendant undue burden or unnecessary expense, the court may limit the participation by the person in the litigation.

(3) If the Government elects not to proceed with the action, the person who initiated the action shall have the right to conduct the action. If the Government's so requests, it shall be served with copies of all pleadings filed in the action and shall be supplied with copies of all deposition transcripts (at the Government's expense). When the person proceeds with the action, the court, without limiting the status and rights of the person initiating the action, may nevertheless

permit the Government to intervene at a later date upon a showing of good cause.

(4) Whether or not the Government proceeds with the action, upon a showing by the Government that certain actions of discovery by the person's initiating the action would interfere with the Government's investigation or prosecution of a criminal or civil matter arising out of the same facts, the court may stay such discovery for a period of not more than 60 days. Such a showing shall be conducted in camera. The court may extend the 60-day period upon a further showing in camera that the Government has pursued the criminal or civil investigation or proceedings with reasonable diligence and any proposed discovery in the civil action will interfere with the ongoing criminal or civil investigation or proceedings.

(5) Notwithstanding subsection (b), the Government may elect to pursue its claim through any alternate remedy available to the Government, including any administrative proceeding to determine a civil money penalty. If any such alternate remedy is pursued in another proceeding, the person initiating the action shall have the same rights in such proceeding as such person would have had if the action had continued under this section. Any finding of fact or conclusion of law made in such other proceeding that has become final shall be conclusive on all parties to an action under this section. For purposes of the preceding sentence, a finding or conclusion is final if it has been finally determined on appeal to the appropriate court of the United States, if all time for filing such an appeal with respect to the finding or conclusion has expired, or if the finding or conclusion is not subject to judicial review.

(d) **Award to qui tam plaintiff.** (1) If the Government proceeds with an action brought by a person under subsection (b), such person shall, subject to the second sentence of this paragraph, receive at least 15 percent but not more than 25 percent of the proceeds of the action or settlement of the claim, depending

upon the extent to which the person substantially contributed to the prosecution of the action. Where the action is one which the court finds to be based primarily on disclosures of specific information (other than information provided by the person bringing the action) relating to allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government Accounting Office report, hearing, audit, or investigation, or from the news media, the court may award such sums as it considers appropriate, but in no case more than 10 percent of the proceeds, taking into account the significance of the information and the role of the person bringing the action in advancing the case to litigation. Any payment to a person under the first or second sentence of this paragraph shall be made from the proceeds. Any such person shall also receive an amount for reasonable expenses which the court finds to have been necessarily incurred, plus reasonable attorneys' fees and costs. All such expenses, fees, and costs shall be awarded against the defendant.

(2) If the Government does not proceed with an action under this section, the person bringing the action or settling the claim shall receive an amount which the court decides is reasonable for collecting the civil penalty and damages. The amount shall be not less than 25 percent and not more than 30 percent of the proceeds of the action or settlement and shall be paid out of such proceeds. Such person shall also receive an amount for reasonable expenses which the court finds to have been necessarily incurred, plus reasonable attorneys' fees and costs. All such expenses, fees, and costs shall be awarded against the defendant.

(3) If the Government does not proceed with the action and the person bringing the action conducts the action, the court may award to the defendant its reasonable attorneys' fees and expenses if the defendant prevails in the action and the court finds that the claim of the person bringing the action was clearly frivolous, clearly vexatious, or brought primarily for purposes of harassment.

(e) **Certain actions barred.** (1) No court shall have jurisdiction over an action brought by a former or present member of the armed forces under subsection (b) of this section against a member of the armed forces arising out of such person's service in the armed forces.

(2)(A) No court shall have jurisdiction over an action brought under subsection (b) against a Member of Congress, a member of the judiciary, or a senior executive branch official if the action is based on evidence or information known to the Government when the action was brought.

(B) For purposes of this paragraph, "senior executive branch official" means any officer or employee listed in [section] paragraphs (1) through (8) of section 101(f) of the Ethics in Government Act of 1978 (5 U.S.C. App.).

(3) In no event may a person bring an action under subsection (b) which is based upon allegations or transactions which are the subject of a civil suit or an administrative civil money penalty proceeding in which the Government is already a party.

(4)(A) No court shall have jurisdiction over an action under this section based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government Accounting Office report, hearing, audit, or investigation, or from the news media, unless the action is brought by the Attorney General or the person bringing the action is an original source of the information.

(B) For purposes of this paragraph, "original source" means an individual who has direct and independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the Government before filing an action under this section which is based on the information.

(f) Government not liable for certain expenses. The Government is not liable for expenses which a person incurs in bringing an action under this section.

(g) Fees and expenses to prevailing defendant. In civil actions brought under this section by the United States, the provisions of section 2412(d) of title 28 shall apply.

(h) Any employee who is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment by his or her employer because of lawful acts done by the employee on behalf of the employee or others in furtherance of an action under this section, including investigation for, initiation of, testimony for, or assistance in an action filed or to be filed under this section, shall be entitled to all relief necessary to make the employee whole. Such relief shall include reinstatement with the same seniority status such employee would have had but for the discrimination, 2 times the amount of back pay, interest on the back pay, and compensation for any special damages sustained as a result of the discrimination, including litigation costs and reasonable attorneys' fees. An employee may bring an action in the appropriate district court of the United States for the relief provided in this subsection.

(As amended Oct. 27, 1986, P. L. 99-562, §§ 3, 4, 100 Stat. 3154. 3157: Nov. 19, 1988, P. L. 100-700, § 9, 102 Stat. 4638: May 4, 1990, P. L. 101-280, § 10(a), 104 Stat. 162.)

§ 3731. False claims procedure.

(a) A subpena requiring the attendance of a witness at a trial or hearing conducted under section 3730 of this title may be served at any place in the United States.

(b) A civil action under section 3730 may not be brought—

(1) more than 6 years after the date on which the violation of section 3729 is committed, or

(2) more than 3 years after the date when facts material to the right of action are known or reasonably should have been known by the official of the United States charged with responsibility to act in the circumstances, but in no event more than 10 years after the date on which the violation is committed,

whichever occurs last.

(c) In any action brought under section 3730, the United States shall be required to prove all essential elements of the cause of action, including damages, by a preponderance of the evidence.

(d) Notwithstanding any other provision of law, the Federal Rules of Criminal Procedure, or the Federal Rules of Evidence, a final judgment rendered in favor of the United States in any criminal proceeding charging fraud, or false statements, whether upon a verdict after trial or upon a plea of guilty or nolo contendere, shall estop the defendant from denying the essential elements of the offense in any action which involves the same transaction as in the criminal proceeding and which is brought under subsection (a) or (b) of section 3730.
(As amended Oct. 27, 1986, P. L. 99-562, § 5, 100 Stat. 3158.)

§ 3732. False claims jurisdiction.

(a) Actions under section 3730. Any section under section 3730 may be brought in any judicial district in which the defendant or, in the case of multiple defendants, any one defendant can be found, resides, tranacts business, or in which any act proscribed by section 3729 occurred. A summons as required by the Federal Rules of Civil Procedure shall be issued by the appropriate district court and served at any place within or outside the United States.

(b) Claims under state law. The district courts shall have jurisdiction over any action brought under the laws of any State for the recovery of funds paid by a State or local government if the action arises from the same transaction or occurrence as an action brought under section 3730.

(Added Oct. 27, 1986, P. L. 99-562, § 6(a), 100 Stat. 3158.)

§ 3733. Civil investigative demands

(a) In general. (1) Issuance and service. Whenever the Attorney General has reason to believe that any person may be in possession, custody, or control of any documentary material or information relevant to a false claims law investigation, the Attorney General may, before commencing a civil proceeding under section 3730 or other false claims law, issue in writing and cause to be served upon such person, a civil investigative demand requiring such person—

(A) to produce such documentary material for inspection and copying,

(B) to answer in writing written interrogatories with respect to such documentary material or information,

(C) to give oral testimony concerning such documentary material or information, or

(D) to furnish any combination of such material, answers, or testimony.

The Attorney General may not delegate the authority to issue civil investigative demands under this subsection. Whenever a civil investigative demand is an express demand for any product of discovery, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General shall cause to be served, in any manner authorized by this section, a copy of such demand upon the person from whom the discovery was obtained and shall notify the person to whom such demand is issued of the date on which such copy was served.

§ 3333(a)-(2)-(l)—[Omitted as provisions not involved in this case.]

1958 Water Supply Act 43 U.S.C 390b et. seq.

§ 390b. Development of water supplies for domestic, municipal, industrial, and other purposes

(a) Declaration of policy

It is hereby declared to be the policy of the Congress to recognize the primary responsibilities of the States and local interests in developing water supplies for domestic, municipal, industrial, and other purposes and that the Federal Government should participate and cooperate with States and local interests in developing such water supplies in connection with the construction, maintenance, and operation of Federal navigation, flood control, irrigation, or multiple purpose projects.

(b) Storage in reservoir projects; agreements for payment of cost of construction or modification of projects

In carrying out the policy set forth in this section, it is hereby provided that storage may be included in any reservoir project surveyed, planned, constructed or to be planned, surveyed and/or constructed by the Corps of Engineers or the Bureau of Reclamation to impound water for present or anticipated future demand or need for municipal or industrial water, and the reasonable value thereof may be taken into account in estimating the economic value of the entire project: *Provided,* That the cost of any construction or modification authorized under the provisions of this section shall be determined on the basis that all authorized purposes served by the project shall share equitably in the benefits of multiple purpose construction, as determined by the Secretary of the Army or the Secretary of the Interior, as the case may be: *Provided further,* That before construction or modification of any project including water supply provisions for present demand is initiated, State or local interests shall agree to pay for the cost of such provisions in accordance with the provisions of this section: *And provided further,* That not to exceed 30 per centum of the total estimated cost of any project may be allocated to anticipated future

demands where State or local interests give reasonable assurances, and there is reasonable evidence, that such demands for the use of such storage will be made within a period of time which will permit paying out the costs allocated to water supply within the life of the project: *And provided further,* That the entire amount of the construction costs, including interest during construction, allocated to water supply shall be repaid within the life of the project but in no event to exceed fifty years after the project is first used for the storage of water for water supply purposes, except that (1) no payment need be made with respect to storage for future water supply until such supply is first used, and (2) no interest shall be charged on such cost until such supply is first used, but in no case shall the interest-free period exceed ten years. The interest rate used for purposes of computing interest during construction and interest on the unpaid balance shall be determined by the Secretary of the Treasury, as of the beginning of the fiscal year in which construction is initiated, on the costs of the computed average interest rate payable by the Treasury upon its outstanding marketable public obligations, which are neither due nor callable for redemption for fifteen years from date of issue. The provisions of this subsection insofar as they relate to the Bureau of Reclamation and the Secretary of the Interior shall be alternative to and not a substitute for the provisions of the Reclamation Projects Act of 1939 (53 Stat. 1187) [43 U.S.C.A. § 485 et seq.] relating to the same subject.

(c) Application to other laws

The provisions of this section shall not be construed to modify the provisions of section 701-1 of title 33 and section 390 of this title, as amended and extended, or the provisions of sections 372 and 383 of this title.

(d) Approval of Congress of modifications of reservoir projects

Modifications of a reservoir project heretofore authorized, surveyed, planned or constructed to include storage as provided

in subsection (b) of this section which would seriously affect the purposes for which the project was authorized, surveyed, planned, or constructed or which would involve major structural or operational changes shall be made only upon approval of Congress as now provided by law.

(Pub.L. 85-500, Title III, § 301. July 3, 1958, 72 Stat. 319; Pub.L 97-88. § 1 July 20, 1961, 75 Stat. 210.)

MEMO FOR RECORD

Re: Enlarged Warm Springs Dam Project, and proposed Draft Contract for Repayment of Costs under 1958 Water Supply Act Between U.S. and Sonoma County Water Agency

1. In my legal opinion, the 1958 Water Supply Act, 43 U.S.C. 390 et seq., and the authorizing act for the Warm Springs Dam Project, P.L. 87-874, requires that the "entire cost" allocated to water supply storage shall be repaid to the U.S. not later than 50 years after the project is first used for the storage of water supply purposes.

2. Also, there is no legal basis for authorizing the deferral of interest payments allocated to future water supply beyond ten years after the plant in service date. I have examined other water supply contracts which conform with the 1958 Water Supply Act—e.g. contract between the U.S. and McGee Creek Authority on McGee Creek Project. This 1979 contract is consistent with the repayment provisions of the 1958 Water Supply Act. In contrast, the proposed draft contract between the U.S. and the Sonoma County Water Agency on the enlarged Warm Springs Dam Project, in my opinion, does not reflect repayment terms which are consistent with the 1958 Water Supply Act. As mentioned, it is my opinion that 43 U.S.C. 390(b) requires repayment in a period not to exceed 50 years. It states "and provided further that the entire amount of construction costs, including interest during construction, allocated to water supply shall be repaid within the life of the project *but in no event to exceed 50 years after the project is first used for* the storage of water for water supply purposes, except that (1) no payment need be made with respect to storage for future water supply until such supply is first used, and (2) no interest shall be charged on such cost until such supply is first used, but in no case shall the interest free period exceed ten years." In my opinion, there is no exception to the 50 year repayment *term,* and the exception, as stated, applies only to the initiation of payments for future water supply. The statute still requires that the *term,* of repayment for the "entire

amount" shall "*in no event* exceed fifty years after the project is first used for the storage of water for water supply purposes." The "entire amount" covers future water supply, and local interests are required to provide evidence that its demands for water supply will be made within a period to repay the "entire amount in a period not to exceed 50 years after the project is put into operation. This has been thoroughly discussed with the District Engineer who will be entering into the contract on behalf of the U.S. and we understand that we have a difference of opinion. As I understand the District Engineer's interruption [sic], he believes that the statute provides for an exception to the 50 year repayment term for the "entire amount," and that this entire amount may be paid back well beyond 50 years by applying a 50 year payment period to various future blocks composing the "entire amount," by staggering the initiation of the payment period for the various amounts associated with the blocks that compose the "entire amount." The District Engineer believes that the payment period may extend beyond 50 years, and that the *payment* of interest may likewise be deferred beyond the 10 year period until use of future supply is initiated provided interest starts occurring on the 10th year. The interest rate on the project is 3.2% as determined by Engineering. As mentioned, I do not agree with the District Engineer's interpretation which I believe provides for exceptions not provided for by the statute, and which are inconsistent with the statute. Conversely, the District Engineer does not agree with my interpretation. While recognizing this difference of opinion, it is further noted that the District Engineer's interpretation as reflected in the above-mentioned Warm Springs draft contract is probably *not* inconsistent with the previous position of the Corps General Counsel's office (OCE) and the draft contract format furnished by OCE.

3. It is my understanding that the District Engineer plans to submit this matter to the General Counsel's Office for his review since this matter will eventually be approved by higher authority. Nevertheless, based on the matters mentioned above, I do not agree with the OCE—District Engineer interpretation on this and related matters.

4. In this regard, the 1962 authorizing legislation, P.L. 87-874, approved the project in accordance with House Document 547 which provided in that report for a cost allocation on a project whose total storage was 277,000 A.F. and 132,000 A.F. out of that total was for water supply storage.

5. In my opinion, the Chief of Engineers' apparent decision to increase the total storage and water conservation storage to 381,000 A.F. and 212,000 A.F. respectively without Congressional authorization does not accord with 43 U.S.C. 390(b)(d) which provides that: "Modification of a reservoir project heretofore authorized, planned, or constructed to include storage as provided in subsection (b) of this section which would seriously affect the purposes for which the project was authorized, surveyed, planned, or constructed, or which would involve major structural or operational changes shall be made only upon the approval of Congress as now provided by law. "By passing 43 U.S.C. 390," Congress limited the Chief of Engineers authority to make discretionary changes on water supply storage projects, and the broad discretionary authority applicable to flood control purposes does not provide a basis to disregard the statutory duties imposed in 43 U.S.C. 390(b)(d). This view was also recognized by Division Planning in its memo attached hereto for review.

6. However, as a result of the former Chief of Engineers previous decision, a report with a cost allocation for the enlarged project has not been submitted to Congress for its authorization. As mentioned, the cost allocation for the authorized project referred to in House Document 547 was submitted to Congress when it authorized the smaller project in accordance with that report. The Supreme Court and the 9th Circuit Court of Appeals ruled that appropriation of funds for a project does not constitute authorization of a project, and that it can not be inferred that a project is authorized from appropriations. Libby Rod and Fun Club v. Poteat 594 F. 2d 742 1979, and T.V.A. v. Hill 437 U.S. 153, 98 S.Ct. 2279, 57 L. Ed. 2d 117 1978. The Chief of Engineers' decision that he had discretionary authority to enlarge the

Warm Springs Project was made prior to the above-mentioned court decisions. In my opinion, the fact that the Corps may have sought and received appropriations for an enlarged project would not constitute the required authorization based on the court decisions mentioned above. Consequently, based on the former Chief of Engineers previous decision, the San Francisco District is now in a position of undertaking an enlarged project which has not been submitted to Congress for its authorization.

7. The San Francisco District (Engineering) has proposed that Sonoma County Water Agency reply [sic] to the U.S. 27.8% of the Construction costs for enlarged Warm Springs Dam. This is less than the Sonoma County's cost share of 29% associated with the smaller project. The enlarged project has a relatively higher percentage of storage allocated to water supply than the smaller project, and the proposed contract provides for Sonoma County's right to utilize .02% of the total storage space for water conservation storage (adjusted for sediment). Since a cost allocation for the enlarged project has not been included in an authorization report for Congressional approval as was the case for the smaller project, there is certainly no assurance that Congress would approve the cost allocation associated with the larger project if an authorization report were submitted to Congress in accordance with 43 U.S.C. 390b. A 1% difference in the cost allocation share is over $3 million based on fiscal 1981 estimated prices.

8. Also, of the total increase in storage (104,000 A.F.) for which enlargements in the project are proposed and being made, 76% of that storage increase is for water supply storage.

9. For the Corps to administratively enlarge the Warm Springs Project, which enlargements are based on increasing the water supply in the smaller project by 60% (80,000 A.F./132,000 A.F.), and to reduce the cost percentage to Sonoma County associated with the enlarged project, and to undertake such actions without Congressional authorization, is a matter which I believe should be seriously reconsidered. Again, in my opinion, the above-mentioned court decisions, and 43 U.S.C 390(b)(d)

would require Congressional authorization for the enlarged Warm Springs Project. If the District Engineer does not agree with my legal interpretations, his decision may not be inconsistent with the previous decision of the former Chief of Engineers as mentioned above. This is a further recognition of my differences of opinion on this matter. The District Engineer has been fully apprised of my opinions, the court decisions mentioned above. Also, this and related matters have been discussed with the District Engineer, Warm Springs Dam Project Coordinator and others.

JIM HAGOOD
Assistant District Counsel

CF: **Col. Bazilwich**
District Engineer

Cpt Scott Moseley
Warm Springs Dam
Project Coordinator

DISPOSITION FORM

REFERENCE OR OFFICE SYMBOL	SUBJECT
SPNOC	Draft Warm Springs Dam Contract

TO	FROM	DATE
Capt. Scott Moseley Engineering Div.	Assistant District Counsel	30 Nov 1981

In response to your request for "correction" and/or comments on the *draft* contract between the U.S. and the Sonoma County Water Agency (SCWA) on the Warm Springs Dam Project and S.C.W.A.'s repayment obligations, the following is provided:

1. As you know through discussions, it is my opinion that the repayment terms being proposed by S.C.W.A. and incorporated into the draft contract are not in accordance with the statutory repayment requirements of the 1958 Water Supply Act, 43 U.S.C. 390 et. seq. Since this matter has been discussed extensively, there is no reason to comment further other than to note that in my opinion the terms for repayment to the U.S. are not consistent with the requirements of the 1958 Water Supply Act. The District Engineer and I have acknowledged that we have a difference of opinion on this matter.

2. It is suggested that the definition of "annual anniversary date", page 26, item 1, be changed as per the attached.

3. Also, please note the attached document on the distribution of the sediment reservation.

/s/ JIM HAGOOD

JIM HAGOOD

* MFR — In meeting on 30 Nov., 1981 with Col. Bazilwich, District Engineer, Jay Soper, Chief of Engineering San Francisco District, and Capt. Mosely, Warm Springs Dam Project

Coordinator, I advised them that in my opinion the contract being proposed by the District, and proposed by Engineering did not adhere to the repayment requirements of the 1958 Water Supply, and that I would not prepare such a contract since in my opinion I did not agree with it. At that point Col. Bazilwich advised me that if he tells me to do something I have to do it even if I disagree with it on legal grounds. Also I was advised by Mr. Soper that "Lawyers don't have any ethics." I again stated that in my opinion the proposed contract did not comply with the 1958 Water Supply Act and that I was entitled to my opinion.

JIM HAGOOD
30 Nov 1981

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* Handwritten copy

SPNOC
Col. Paul Bazilwich, Jr.

[LETTERHEAD]

25 March 1982

Col. Paul Bazilwich, Jr.
District Engineer, and
Contracting Officer on Warm Springs Dam Project
211 Main Street, 9th Floor
San Francisco, Calif.

Re: Enlarged Warm Springs Dam Project, Sonoma County, California, Repayment Rights of U.S. for Water Supply Storage for Municipal and Industrial Storage under 1958 Water Supply Act, 43 U.S.C. 390 et seq.

Dear Col. Bazilwich:

This is in regards to the above mentioned matter.

In my legal opinion, the repayment contract which you have directed with the Sonoma County Water Agency (S.C.W.A.) on the enlarged Warm Springs Dam Project (W.S.D.P.) does not comply with the 1958 Water Supply Act, 43 U.S.C. 390(b) et seq., and substantially understates the amounts required to be repaid to the U.S. by law. The total estimated cost for the Warm Springs Dam Project is $312 million. This is based on 1982 cost data which includes actual costs incurred and remaining projected costs.

You have made "command decisions" concerning the above-mentioned draft contract for the W.S.D.P., and have ordered and directed repayment provisions for the S.C.W.A. which provides for: (1) S.C.W.A.'s repayment of 27% of the total project costs of the enlarged W.S.D.P. based on a 1967 cost

allocation in the San Francisco District Engineering Department's General Design Memorandum; (2) a repayment term beyond 50 years after the project is put into operation, and (3) deferred *payment* of interest (3⅛%) beyond 10 years after the date the project is put into operation. As you know, I have totally disagreed with your above mentioned decisions, and have indicated to you that in my opinion they do not comply with the statutory requirements of the 1958 Water Supply Act 43, U.S.C. 390(b) et seq.

In several meetings with you, I have advised you of my objections to your decisions, and indicated to you that I would not prepare, participate in, or approve a draft repayment contract reflecting your decisions which substantially understate the amount of repayment to the U.S. required by law. My legal objections to your actions, directives, and decisions on the modifications enlarging the Warm Springs Dam Project and the draft repayment contract are based on the following:

a. Congress authorized the W.S.D.P. pursuant to P.L. 87-874 in accordance with House Document 547 which provided for the Sonoma County Water Agency (S.C.W.A.) to repay the U.S. the percentage of the total project costs for a project with 132,000 acre feet (A.F.) of water supply storage for municipal and industrial purposes (M. and I.) based on conditions prevailing at the time of construction and actual costs incurred, and the furnishing of assurances satisfactory to the Secretary of the Army for repayment of such costs.

b. Congress approved the W.S.D.P. with 132,000 A.F. of water supply storage for M. and I. purposes based on the above and the repayment amount for that project prevailing prior to construction was in the 1964 contract and was *29%* of the total project costs. This repayment amount was later reduced by the Corps Engineering Department in its General Design Memo prepared between 1967-1969 (hereinafter referred to as 1967

GDM). See attached cost allocation in GDM (Incl. 1). Congress never approved this reduction, nor amended P.L. 87-874 to allow for such a reduction for a 132,000 A.F. water supply storage for M. and I. purposes in the W.S.D.P.

c. Also, in connection with reducing the repayment amount for a 132,000 A.F. water supply storage project (to 24%), the San Francisco District's Engineering Department in its 1967 GDM prepared as an alternative the substantial modification of the authorized project by increasing the water supply storage for M. and I. purposes by 60% to 212,000 A.F. and further effectively reduced S.C.S.W.s repayment obligation for an enlarged water supply storage project for M. and I. purposes. The total increase in storage proposed was 104,000 A.F. and of that amount 77% or 80,000 A.F. was for added water supply storage. The cost sharing percentage you are proposing in the contract is 27.76. Any reference to 27% also refers to 27.76, and 27% is used for convenience without repeating the decimal points. The reduction to 27% by the Corps Engineering Department (not Congress) for the enlarged project was related to and based on the above-mentioned previous reduction to 24% from 29% (based on the 1964 contract) for the 132,000 A.F. project authorized by Congress. The total storage for this multi-purpose project for flood control, water supply, and recreation, was 277,000 A.F., and of that amount 132,000 A.F. was for water supply storage. In the enlarged W.S.D.P., which has not been submitted to the full Congress in accordance with 43 U.S.C. 390(b) for its approval, the total storage being built into that project is 381,000 A.F., and 55% of that amount or 212,000 A.F. is for water supply storage. The modification enlarging the water supply storage for M. and I. on a percentage basis) and simultaneously reducing the repayment obligation of the S.C.W.A. was *not* approved by Congress in accordance with 43 U.S.C. 390(b)(d), or pursuant to an amendment to P.L. 87-874. Appropriations for an enlarged project do

not constitute an authorization. *T.V.A. v. Hill* 437 U.S. 153, 1978, and *Libby Rod and Gun Club v. Poteat* 594 F 2d 749, 1979.

d. Despite the Engineering Department's major modifications, enlarging the project and the reducing the repayment obligations to the United States which were different from that approved by Congress pursuant to P.L. 87-874, the Corps has not submitted the modifications (modifications in project and modifications in repayment obligations) to Congress for approval as required by 43 U.S.C. 390(b)(d), due to the positions taken in the 1967 GDM and the Corps' comments on that document.(1) Furthermore, you have decided in connection with your "command decisions" not to forward or submit this decided matter to the *full* Congress for its approval pursuant to the above statutory requirements. In my opinion, the major modifications which you are proposing and which effectively reduce the S.C.W.A. repayment obligations are subject to 43 U.S.C. 390(b)(d), and I have advised you of this. You disagree with me on this matter, as well as other matters.

e. After the project was enlarged in the design stage, and the Engineering Department effectively reduced the S.C.W.A. repayment obligation (despite the addition of 80,000 A.F. of

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(1) If the Corps submits the major modifications, which were indicated as "major changes" by the former Chief of Engineering (OCE), to the full Congress for its approval in accordance with 43 U.S.C. 390(b) and it relies on the 1967 GDM and cost allocation, then that document would become the Congressional document for purposes of authorization. If the Corps is going to continue to rely on the 1967 GDM cost allocation, it should be submitted to the full Congress. Project modifications authorized by Congress pursuant to Public Law (P.L.) are numerous; e.g., note P.L. 94-587. Sections 194 and 196. Engineering does *not* agree that modifications require authorization and is of the opinion that major modifications can be made in the design stage as was done in the case of the W.S.D.P. *without* Congressional authorization.

water supply storage for M. and I. purposes), the project costs *increased over 240 million dollars.*

f. The Chief of Engineers apparently assumed that he had discretionary authority to enlarge the project based on the representations of the San Francisco District Engineering Department in the 1967 GDM that the cost to enlarge the project would only be *2.8 million dollars* over that for the smaller and basic authorized project. (Note inclosed table of cost allocation for smaller authorized project — first cost $67.2 million (Incl. 2) and table for enlarged project with first cost of $70 million (Incl. 3)). Also, this is reflected in the Chief of Engineers May 15, 1967 letter to the Public Works Committee. However, this letter does not disclose that the percentage of repayment for an enlarged project was not increased, and the cost increase represented was primarily due to inflation.

g. It is now evident that the cost data in the 1967 GDM substantially understated the actual costs to enlarge the project, and the data was based on an incomplete design necessary for the assured earthquake safety of an enlarged water supply project. While the project costs have increased due to inflation associated with design delays, those delays were occasioned by the design matters connected with the earthquake safety for an enlarged project, and any increases in costs through inflation or design changes would nevertheless be attributed to the enlarged water supply storage project. These changes resulted from the use of a dynamic analysis method not used on the smaller project prior to the 1967 GDM. Also, the State of California engaged in an extensive review and comment on the enlarged project under its review standards due to the earthquake safety concerns expressed on the project from the California Department of Mines and Geology, and others. The design, supervision, and administration costs for the enlarged project have risen to an amount over $42 million (based on 1 January 1982 data) which is

equivalent to the *total* costs for the project prior to its enlargement.(2)

h. Your decision to direct a repayment obligation of 27% for the S.C.W.A. for the enlarged project based on the 1967 GDM cost allocation which represented a 2.8 million dollar cost increase for the enlarged project, when you know that the actual costs for that enlargement have increased many times that amount does not accord with P.L. 87-874, nor is it in accordance with 43 U.S.C. 390(b), et. seq. Your decision directing that repayment obligation of 27% be incorporated into a draft contract without performing a new allocation based on accurate and current costs is not in accordance with the above mentioned laws. Therefore, it appears to me that you have violated your mandatory statutory duties to: (1) Submit the above mentioned modification and repayment obligations for the enlarged project to Congress in accordance with 43 U.S.C. 390(b)(d), and (b) to prepare a cost allocation based on accurate and current cost data for the enlarged project which allocates to the S.C.W.A. its share of the costs for the enlarged project with the added water supply storage being incorporated into that project.

i. Although Corps District personnel have advised you that a current accurate cost allocation should be prepared, you have declined to have one prepared. Also, the Chief of Engineers Office forwarded a letter to the District dated 22 May 1981 which stated: "A new cost allocation is required." It is my understanding that Mr. Riddle, former assistant Chief of Engineering for the District urged you not to have a cost allocation performed

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(2) Also, the 12-fold increase in recreation costs, would cause a substantial decrease in the *net benefits* for recreation causing a major revision in the distribution of joint costs. If this was accurately reflected in a current and proper cost allocation, the percentage distribution of joint costs to water supply storage would increase significantly due to the decrease in net benefits for recreation.

based on accurate and current cost data, and persuaded you to use the cost sharing percentage (27%) contained in the 1967 GDM. Also, this reflects the position of Mr. Pape, former Chief of Engineering for the District.

j. P.L. 87-874, 43 U.S.C. 390 et seq., and all arrangements with the S.C.W.A. for water supply storage whether based on previous assurances or contracts provide that the cost allocation is subject to adjustment to reflect actual costs, incurred costs, and current cost data. If the San Francisco District's Engineering Department has substantially understated costs previously, then this should be timely corrected in an accurate and current cost allocation. The U.S. is not bound by inaccurate and understated costs, and the cost sharing requirements are based on an allocation which is accurate and contains current cost data. However, if the Corps does not timely advise the S.C.W.A. of an adjustment based on the true costs, the repayment assurances of S.C.W.A. may be in question, and may be illusory.

k. Your command decision not to have an accurate cost allocation prepared based on accurate and current data and a proper allocation to water supply storage may result in an invalidation of the S.C.W.A. repayment assurances. As you know, as a Contracting Officer, currently expending funds subject to repayment, your decision not to have a current, and accurate cost allocation prepared, and to delay such an allocation until after the completion of construction could be viewed as a coercive attempt to force on the U.S. a repayment percentage of 27% based on the 1967 GDM cost allocation, even though it may substantially understate the true repayment obligation to the U.S. Also, this could be viewed as an attempt to create coercive deficiences [sic] for the substantial cost increases. Using the 27% cost sharing percentage based on the inaccurate 1967 GDM cost allocation, and applying that percentage to the current total costs of 312 million dollars would merely compound and perpetuate the errors

in the 1967 GDM. Although using that method may give the appearance of a cost allocation from a superficial review, it would result in substantially understating the cost repayment to the U.S. based on a proper cost allocation, and it would result in the misdistribution of costs subject to repayment to the U.S. I have been advised by knowledgeable sources that if a current and accurate cost allocation was performed, that S.C.W.A.'s repayment obligation would increase at least $60 million over its cost allocation based on the inaccurate 1967 GDM. Thus S.C.W.A.'s cost share may be over $145 million rather than the approximately $86 million based on the 27% total repayment obligation. If the 1967 GDM allocation is inaccurate, (and there is no doubt that it is), then S.C.W.A.'s repayment assurances may be invalid and it would be inaccurate to represent that S.C.W.A. has provided adequate, valid, and full repayment assurances. Also, note *EDG v. John Marsh* 5th Cir. No. 89.3915, 1981. Repayment rights of the U.S. can not be waived nor is the U.S. bound by actions exceeding statutory authority or violating statutory duties. There is a requirement under 43 U.S.C. 390 et seq. to obtain *valid* assurances of repayment based on accurate cost data and a proper allocation before proceeding with and continuing with construction, and before expending funds, and imposing costs on the U.S. subject to repayment.

l. Your decision to extend repayments *beyond 50 years* after the project is put into operation is questionable, and in my opinion does not conform to the statutory repayment requirements of 43 U.S.C. 390(b) et seq. for several reasons:

a. It is probable that a new and proper cost allocation based on accurate and current costs would indicate the S.C.W.A. repayment obligation is substantially beyond 30%. Although the costs for water supply storage may be beyond 30%, it would be a gross misinterpretation of the law to put an artificial cap on S.C.W.A.'s cost allocation to keep it

under 30% for the purpose of deferring payments to the U.S. and extending the repayment period beyond 50 years *after* the project is put into operation. The payment term proposed extends 60 years after the project is scheduled to be put into operation for storage, now scheduled for 1983; i.e., 50 years beyond 1993 amounts to 60 years.

b. Despite OMB's objections to the use of a repayment scheme which would extend repayment for the "entire amount" beyond 50 years contrary to the requirements of 43 U.S.C. 390 resulting in a non-enforcement of U.S. repayment rights by the Corps, you propose to disregard those objections. This may result in a violation of the statute, and you were requested to have this matter resolved between the Secretary of the Army and OMB. Extending repayments 10 years (the interest rate is 3⅛%) beyond the statutory 50 year period for the "entire amount" would result in repayments in depreciated dollars resulting in the U.S. being paid back substantially less in terms of real dollars which amounts would increase even further if the average rate of inflation increased over that extended period. Since the U.S. would not be paid back within the statutory 50 year period, the non-enforcement of those statutory repayment rights would result in the U.S. losing millions of dollars (in real fixed purchasing power) each year on this project alone. Congress has not amended 43 U.S.C. 390(b) to authorize a repayment period for the "entire amount" to extend 60 years beyond the period the project is first used for the storage of water. The W.S.D.P. (the Project) will store water in 1983. There are no exceptions to the 50 year payment period in the statute which provides that the "entire amount" . . . shall be repaid within the life of the Project but *in no event to exceed 50 years* after the project is first used for the storage of water for water supply purposes. While payments do not need to be initiated for future water supply

after the Project is used for the storage of water, the statute clearly provides that the "entire amount" shall be repaid 50 years from the *date* the *project* is first used for the storage of water for water supply purposes. The statute has not been amended to allow for a period beyond 50 years, and any administrative actions purporting to extend the 50 year period would be contrary to the *mandatory* repayment period of 50 years for the "entire amount."

m. Also, you propose to defer *payment* of interest (3⅛%) beyond the 10 years prescribed by 43 U.S.C. 390(b). In my opinion, this is questionable and would add to the already substantial understatement of repayment obligations to the U.S. resulting from your "command directives."

I regret having to write this letter to you. However, it is required. Further discussions with you apparently would not resolve my legal objections to your actions, and it appears that it is your intention to rely on an inaccurate cost allocation for a 27% repayment percentage, and to proceed as noted above. Therefore, for the reasons mentioned above, I respectively decline to support or follow your command directives noted above, and I have not, and will not participate in or prepare any draft contract provisions or other similar legal documents which reflect your command directives which I have objected to on the legal grounds noted above.

Pursuant to Army Procurement Procedure 1-451(c), this letter should be forwarded to the Secretary of the Army so that he can be put on notice of the unresolved legal objections to your actions. This will be done either along with the draft contract reflecting your directives which I object to, or if this is further delayed, it will be timely forwarded separate from your draft contract because of the distinct possibility that the S.C.W.A. repayment assurances are inadequate based on the cost sharing percentage (27%) derived from an inaccurate 1967 GDM cost

SPNOC
Col. Paul Bazilwich, Jr.

allocation, and because of the substantial impact this may have on U.S. repayment rights.

Sincerely,

/s/ JAMES M. HAGOOD

JAMES M. HAGOOD
Assistant District Counsel

CF: Custodian of Records of
U.S. Army Corps of Engineers
San Francisco District, Mr. Jan Brevet

Chief, Engineering Division
San Francisco District
Mr. Jay Soper

Warm Springs Dam Contract Files
c/o Mr. Archie Hays, Chief, Procurement
and Supply Div.

Mr. Steve Lingenfelter
District Counsel, San Francisco Dist.

Mr. Martin Dense, Comptroller

CF: Mr. Scott Moseley
Special Assistant on
Warm Springs Project

ATTACHMENT A

[Letterhead]

July 1, 1982

Lt. Gen. J. K. Bratton
Chief Engineer
U.S. Army Corps of Engineers
Washington, D.C. 20314

Dear Lt. Gen. Bratton

On behalf of the City of Ukiah, California, we are writing to object to the provisions of a proposed contract pending your approval between the Corps of Engineers and the Sonoma County Water Agency ("Sonoma" or "Water Agency"). The proposed contract would change Sonoma's repayment obligation for the use of water stored at the Warm Springs Dam Project. Ukiah is particularly concerned with the tendered modification because, despite the fact that it is a *proposal* (which deviates from statutory repayment standards under the Water Supply Act of 1958) it has been relied upon by the Federal Energy Regulatory Commission ("FERC") to deny Ukiah a preliminary permit to develop the hydroelectric potential of the dam at Warm Springs.

Ukiah applied on May 27, 1980 to the FERC for a preliminary permit to study the feasibility of installing hydroelectric facilities at the Warm Springs Dam. Subsequently, on August 25, 1980 Sonoma filed a competing application and urged the FERC to reject Ukiah's application because of an alleged ability to control water releases and maximize electric generation. Sonoma has further indicated that it would restrict water releases to any other entities securing the right to generate

power at the dam and thus minimize the power potential of such a project.

The proposed contract pending your review and approval constitutes the factual predicate for the FERC's denial of Ukiah's permit application. During negotiation of the contract modification, Sonoma submitted a draft to the FERC to bolster its claimed superior generation capability. On the basis of that submittal, the Commission issued an order which granted a preliminary permit to Sonoma and denied Ukiah's application. The FERC relied on the proposed repayment schedule to conclude that it would "permit Sonoma to increase power production at Warm Springs Dam without triggering the pay-back schedule."[1] Therefore, the order concludes that based upon its relationship with the Corps, Sonoma would be able to produce substantially more power at the site than would be possible if Ukiah were the operator of the hydroelectric facility. The Commission's decision is, however, interim inasmuch as rehearing has been granted for further reconsideration of the wisdom of granting the permit to Sonoma on the basis of its bald claims.

Sonoma lacks the authority to operate the project in the manner so claimed. The Water Agency is precluded from increasing stream flows for power generation beyond those releases made incidental to the other stated purposes of the project under its present permit issued by the California Water Resources Control Board. In addition, the Water Agency has been enjoined by the Sonoma County Superior Court[2] from arbitrarily directing releases pending the submittal and approval of a comprehensive plan for coordinated operation of the Warm Springs and Lake Mendocino projects.

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[1] Order Issuing Preliminary Permit and Denying competing Application, Project Nos. 3186 and 3351, 18 FERC §61.108 (1982), mimeo. at 3, see Appendix A.

[2] Peremptory Writ of Mandate issued August 25, 1981, attached hereto as Appendix B.

Ukiah also protests Sonoma's attempt to avoid its repayment obligation under the Water Supply Act of 1958, 43 U.S.C. 390b. The Warm Springs water supply storage contract is subject to the requirements of the 1958 Act and likewise the repayment obligations are subject to those requirements. The existing "Lake Sonoma Water Supply Contract — Warm Springs Dam Project, Dry Creek, Russian River Basin, California," No. DA-04-203-CIVENG-65-21 tracks the repayment provisions of the Act. In contrast, the draft contract runs afoul of the Act's explicit repayment obligation which provides:

> [t]hat the entire amount of construction costs, including interest during construction, allocated to water supply should be paid within the life of the project but *in no event to exceed fifty years after the project is first used for the storage of water* for water supply purposes, except that (1) no payment need be made with respect to storage for future water supply *until such supply is first used,* and (2) no interest shall be charged on such costs until such supply is first used, but it no case shall the interest-free period exceed ten years. 43 U.S.C. 390(b).

The draft contract proposes, however, rather than requiring repayment within fifty years after water storage is initiated and actual repayment upon first use of stored water, that repayment begin in 1993 and extend 49 years therefrom. Thus, the proposed repayment schedule is an attempt by Sonoma to bolster its threat to thwart the success of a Ukiah-operated project by allowing it to withhold water releases without triggering the fifty-year repayment deadline which would otherwise be imposed if the contract followed the statutory repayment schedule. Alternatively, the proposed modification would allow Sonoma to withdraw water from behind the dam before 1992 without initiating the statutory repayment obligation which would otherwise require repayment to begin when "such supply is first used." In short, under either scenario the proposed repayment schedule is an attempt to avoid

the express provisions of the Act solely to advance the interests of Sonoma.

Sonoma's objectives in modifying the terms of its contract with the Corps are clear — to thwart Ukiah's first-filed application[3] in order to obtain a preliminary permit for itself to operate at the Warm Springs Dam. Ukiah is particularly troubled by Sonoma's assertions that it intends to exercise its claimed contract rights to frustrate the optimal development and use of this multipurpose project. The Corps should not allow itself to be a party to such a scheme, especially where, as here, the proposed contract modification is violative of the Water Supply Act of 1958. Indeed, Sonoma by its proposed repayment schedule has indicated that it does not intend to make use of storage blocks 3 and 4 until the years 2000 and 2005, respectively. If hydroelectric generation can be enhanced by releases from the reservoir at Warm Springs prior to 1992, Ukiah stands ready, willing and able to develop an optimal facility and to compensate the United States for use of those blocks for which Sonoma has no present need.[4] Accordingly, Ukiah would welcome the opportunity to meet and discuss with the Corps the sharing of the costs and benefits of the project. The City of Ukiah believes that it is in the public's best interest to make balanced use of the multiple purposes envisioned for Warm Springs. And, in order to realize the benefit of hydroelectric generation before 1992, Ukiah is willing to pay proportionate costs so as to equitably share in the benefits of the project in accordance with the intent and the terms of the 1958 Water Supply Act.

In sum, the City of Ukiah objects to any contract modification which would unlawfully enhance Sonoma's existing water storage rights or which would allow Sonoma to abuse its rights to the detriment of the multiple purposes of the Warm Springs

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[3] The Commission's regulations establish a preference for the first-filed applicant, 18 C.F.R. 4.33(g)(2).

[4] Ukiah would recognize the right of recapture by Sonoma as the need arises.

Project, including the generation of hydroelectric power therefrom, in violation of the provisions of the Water Supply Act of 1958. Ukiah is convinced that the Commission's order denying its preliminary permit application on the basis of an unexecuted contract amendment is unlawful and unsupportable. Ukiah also believes that the proposed contract is unlawful and contrary to the public interest and is committed to pursuing its rights in this matter both before the FERC and if necessary the Federal Courts.

Ukiah therefore requests that the Corps not approve any such contract modification. We further request that we be permitted to discuss with the Corps arrangements for utilization of the project to maximize its hydroelectric potential while balancing the other objectives of the Warm Springs Dam Project as contemplated by the Water Supply Act.

Your attention to this matter is appreciated. If you have any questions, please do not hesitate to contact the undersigned.

Sincerely,

Robert A. O'Neil

Attorney for the
City of Ukiah, California

Enclosure

RAO: FLK: mc

cc: Office of the Chief Engineer, DAEN:CWZG
Brig. Gen. Homer Johnstone, Jr, Division Engineer,
South Pacific Division
Major Thomas Edgerton, District Engineer,
San Francisco District
James P. Botz, Sonoma County Counsel

THE
PRESS
DEMOCRAT

Source
Santa Rosa, Calif., Sunday, Oct. 3, 1982

Pact gives water use to county

By BOB KLOSE

A new contract between the Army Corps of Engineers and Sonoma County has cleared the way for the county to make immediate and full use of Lake Sonoma at Warm Springs Dam without financial penalty.

The contract, fixing the county's repayment schedule for the dam, means taxpayers will have free use of the reservoir for nearly eight years before the county must start making payments to the federal government.

The amended contract, approved last week by county supervisors acting as water agency directors, was signed Friday by Corps officials in Washington, D.C..

Water Agency Chief Engineer Robert Beach, who announced the agreement Friday afternoon during a Santa Rosa meeting of the State Water Commission, said the new plan will allow the county to use as much water as it needs as soon as Lake Sonoma is filled, without triggering a higher payment schedule that was called for under the old agreement.

Except for recreation facilities, the dam is nearly complete and after several years of testing Lake Sonoma is projected to be full in 1985 or 1986.

Beach, who said Rep. Don Clausen, R-Crescent City, informed him of the Corps' decision only minutes before he addressed the state commission, said the new agreement will allow the county to make the most efficient use of the Russian River water system by combining the resources of both Lake Sonoma and Lake Mendocino outside Ukiah.

"It is good for the county of Sonoma and the U.S. government as well," Beach said.

"In the absence of the agreement, we could have been forced to operate (Warm Springs) at a detriment to Lake Mendocino and the Corps' recreation facilities there and it could have been totally detrimental to the government financially," Beach said.

He explained that the old agreement tended to encourage the county to restrain use of Warm Springs and thus lower its payments and ultimate payoff to the government.

Beach has been negotiating the new agreement since 1980 and with the assistance of Clausen wrapped up the deal over the last six months.

"Clausen played more than a key role. In my opinion it would not have been possible without Clausen," Beach said.

Here are some of the contract highlights, as explained by Beach:

- Unlimited use of Lake Sonoma water puts the county in a more favorable position in its contest with the city of Ukiah for rights to generate electrical power at Warm Springs Dam. Ukiah's rights to Warm Springs water would limit its power plant capacity to only 11.7 million kilowatt hours in 1985. Sonoma County now can expect to produce 18.6 million kilowatt hours, a 60 percent increase in capacity. The power will be used to cut water agency power bills and thus water rates.
- The county will be able to provide water to maintain minimum stream flows in the lower Russian River for fish and

wildlife and recreation without increasing the cost of water for urban water customers.

- The ability of Lake Sonoma to meet stream flow and urban demands below Healdsburg will put less strain on supplies in Lake Mendocino. As a result there will be more water left in Lake Mendocino for recreation and for meeting stream flow and agricultural demands between Ukiah and Healdsburg.

- Future requests by water customers, such as Marin Municipal Water District and Redwood Valley Water District in Mendocino County, can be negotiated without causing higher payments to Sonoma County. And water agencies that were not party to the Warm Springs Dam project will be required to pay charges equivalent to the cost of water paid by current water agency customers.

"The reliability of the Russian River as a water supply for both agricultural and urban use will be greatly enhanced." Beach said.

All of these issues with parties interested in a share of Warm Springs water still remain in negotiation, Beach said, but the new agreement puts the county in the position of entertaining requests for more use of the resource without having to face increased payments under the old contract with the Corps.

Sonoma County's share of the cost of the $312 million project is $96.6 million, to be paid off by 2035.

Although the actual county bill does not change under the new agreement, now payments will not increase as use of the water supply increases.

Under the old contract, payments to the Corps were scheduled to begin in 1993 or before if the county started using water from the new reservoir prior to that time.

The repayment formula was based on how much water the county used. The total water supply capacity of the dam was cut

into three equal blocks with the payment increasing as the county entered each additional block of storage space.

The original plan was apparently satisfactory to both the Corps and county when it was adopted in 1964. Since then, however, there have been new demands on Lake Sonoma water by interests who don't face the task of paying off a $96.6 million debt.

For example, although the state Department of Fish and Game's request for Lake Sonoma water for stream flow purposes appeared reasonable it could have forced Sonoma County taxpayers in a higher repayment bracket under the old agreement.

Beach said the new plan will allow the county to meet the Fish and Game demands without damaging its own pocket book.

Here's are the terms of the new agreement:

- The county can use Lake Sonoma water as soon as it is available, 1985 or 1986.
- Payments do not begin until 1993, regardless of the fact the county might begin using water eight years earlier.
- Payments will not increase as the use of water increases.

The county established a penny tax in 1971 to be used to pay off its Warm Springs bill. Beach said that fund now stands at about $2 million and will continue to accumulate and earn interest until payments begin in 1993. Given a reasonable investment return in the meantime, he said, the county should be in a good position to begin payments next decade.

Beach said the annual payment in 1993 is set at $868,000. Annual payments gradually increase to $5.9 million by 2007 when they will remain the same until the mortgage is burned in 2035.

The county is paying 3.225 percent in interest.

Although the new contract was hailed by county officials, it could give rise to "I told you so" charges by anti-dam groups that unsuccessfully opposed the project in two county elections and in the court room.

Part of the dam opponents' campaign centered on contentions the dam and increased water supply would spark uncontrolled urban growth and turn Sonoma County into a sprawling population center.

Dam supporters countered that the contract provisions for higher payments following greater use of the water would curb the county from making premature and growth-inducing use of the reservoir.

The new agreement which gives the county unlimited access to the water at no change in the pricetag eliminates financial restraints on growth.

On the other hand, former county supervisor Brian Kahn, who supported the dam despite a concern over the possibilities of it encouraging growth, said Saturday the new contract will actually eliminate one potential incentive for growth. Had the county been forced to use more water during a drought, Kahn said, it would have permanently raised the cost of water.

Faced with higher water costs, Kahn said, the county would have had to encourage development to pay for the water.

That potential is eliminated by a fixed payment, he said, allowing the county to use water to maintain the level of the Russian River and to cover water needs during a draught.

Kahn is a member of the state Fish and Game Commission.